



## **Small Business Subgroup Interim Report**

### **Subgroup Activity:**

The Small Business Subgroup of the Governor's Commission on Economic Development and Job Creation has met twice since the first full Commission meeting. During the June 3<sup>rd</sup> meeting members discussed the research materials provided, clarified areas of concern and reviewed Virginia's small business demographics. The Subgroup members approved their "Visions Strategies" and identified key stakeholders to reach out to for input and guidance.

At the July 6<sup>th</sup> meeting, the Subgroup members heard reports from the Virginia Department of Business Assistance, the Virginia Small Business Financing Authority and the Department of Labor and Industry. Members discussed their research and progress on further formulating the group's "Visions and Goals" in preparation for the interim report. Subgroup members discussed their meetings with stakeholders, state agencies and the small business community members.

Subgroup members will continue to meet and communicate with key stakeholders as they work towards a comprehensive final report. Stakeholder groups include:

Associated Builders and Contractors, Associated General Contractors, Home Builders Association of Virginia, Farm Bureau, Independent Insurance Agents of Virginia, Metropolitan Business League, National Association of Women in Construction, National Federation of Independent Business, Virginia Agribusiness Council, Virginia Association of Community Banks, Virginia Association of Realtors, Virginia Bankers Association, Virginia Chamber of Commerce, Virginia Association of Counties, Virginia Credit Union League, Virginia Hospitality and Travel Association, Virginia Independent Automobile Dealers Association, Virginia Municipal League, Virginia Nursery & Landscape Association, Virginia Petroleum Convenience & Grocery Association, Virginia Retail Federation and the Virginia Retail Merchants Association.

### **Analysis:**

The SRI conducted a study on behalf of the Virginia Economic Development Partnership (VEDP) titled "Catalyzing Innovation in the Commonwealth." The report analyzed Virginia industries, benchmarked economic and innovative foundations, established potential high-growth technologies, outlined best practices from successful technology investment programs and identified strategic inferences for economic development. While it recognized Virginia's many economic strengths; it also highlighted areas of deficiency including improving Virginia's small business environment.

In 2009, the Wall Street Journal published its annual list of the “Best and Worst States for Small-Business Taxation.” The list was based on 16 different tax measures including: income, poverty, death/inheritance, unemployment, and consumption-based taxes like those on gas and diesel. The top ten best tax systems for small business are: 1) South Dakota, 2) Nevada, 3) Wyoming, 4) Washington, 5) Texas, 6) Florida, 7) Alaska, 8) Colorado, 9) Alabama, and 10) Ohio. Virginia ranked 16<sup>th</sup> on the list.

The Small Business & Entrepreneurship Council also ranks states according to their public policy climates for small business and entrepreneurship in the “Small Business Survival Index 2009: Ranking the Policy Environment for Entrepreneurship Across the Nation.” The Index helps business owners, investors and lawmakers understand the public policy burdens placed on entrepreneurship and small business in the states, and ranks them accordingly. The factors included in the Index – taxes, various regulatory costs, government spending, property rights, health care, energy costs, and others – matter a great deal to the competitiveness of each state and to the well being of small businesses. In terms of their policy environments, the Top-Ten entrepreneur-friendly states under the “Small Business Survival Index 2009” are: 1) South Dakota, 2) Nevada, 3) Texas, 4) Wyoming, 5) Washington, 6) Florida, 7) South Carolina, 8) Colorado, 9) Alabama, and 10) Virginia.

While Virginia is one of the more small-business friendly states, significant work is needed to achieve Governor McDonnell’s goal of making Virginia the “Best State in which to Own and Operate a Small Business.” More attention, resources and support needs to be given to the programs and agencies that serve Virginia’s entrepreneurs. The 230,000 small businesses in Virginia (companies with less than 250 employees) comprise 98% of all existing businesses in Virginia and account for approximately 75% of new job growth in the Commonwealth. They are the heart and soul of Virginia’s economy.

Currently, Virginia has over 35 different state agencies that may touch a small business and over 100 business assistance and regulatory programs. While much of the state aid does not specifically apply to small businesses, several programs are designed to help small businesses grow and prosper.

The main provider of small business assistance programs in Virginia is the Department of Business Assistance (DBA). The DBA provides assistance to small businesses through three primary departments: the Virginia Jobs Investment Program (VJIP), the Virginia Small Business Financing Authority (VSBFA) and the Virginia Business Information Services (BIS).

The VJIP offers assistance to businesses through three primary departments: New Jobs Program, Small Business New Jobs Program, and the Retraining Program. Of these three programs, only the latter two apply to small businesses in the Commonwealth. DBA’s VJIP has small business workforce programs, approaches and information on success rates. Workplace education and training remains a challenge for small businesses due to the cost of setting up and administering these programs. As with the rest of the country, Virginia’s workforce is ever changing. Our workforce development needs should be intertwined with education, continuing education for

existing workers and partnering with our community colleges and universities to help develop a skilled workforce, ready to meet the business community's needs.

As the needs for workforce training change, we need to address and identify areas and adjust how we train for the future. The VJIP and the seminars/workshops of BIS within DBA have very useful input and information on best practices in educating employers. Other agencies such as VEC, DOLI and DEQ also have relevant information for small businesses to use.

The VSBFA is the Commonwealth's economic development financing program. While grants are not available through the Authority, it does provide debt financing assistance to Virginia's established, existing businesses and those looking to expand into Virginia. VSBFA provides direct loans in partnership with bank loans to businesses from appropriations received from a one time Federal grant. VSBFA also provides loan guarantees to support bank loans and administers targeted direct loan programs for other state agencies. The VSBFA's ability to aide Virginia's small businesses is directly tied to the amount of funding received from the General Assembly. There are limited funds available and uncertainty as to what will be available each year. In past budget cycles, funding has been so constrained that some VSBFA programs have been put on hold or eliminated, further reducing the options available to Virginia's small business community.

The DBA also offers several informational services. These programs include: Entrepreneur Express, Virginia Business Information Center, Virginia Business One Stop, One-on-One Business Builder Counseling, and Business Sales Growth Seminars. A lack of funding, established marketing plan and limited staff have left these quality programs without the ability to properly meet the business community's needs. Additionally, multiple other agencies house important reference information, guides to business formation and educational programs for employers. While all of the information is extremely helpful, the lack of coordination and single point of contact can leave the entrepreneur confused and overwhelmed.

DBA's budget has declined 56% over the eight years, including a 51% staff reduction over the past four years. In addition to the reduced services and departmental capabilities, the Department's ability to track, examine, identify, and write grant applications to the Federal government is very limited. Federal grants could help fill financial voids and aid businesses that cannot be served through current means.

### **Vision Strategies:**

To spur entrepreneurship, expand existing businesses and create new jobs, the resources and programs available to Virginia small businesses need significant enhancements. For Virginia to become the best state for small business, economic development strategies and incentives must be aligned to support and encourage all of Virginia's job creators. Business formation and existing business expansion are the largest drivers of job growth in Virginia. While large investments have been made to bolster business recruitment incentives, aid to existing businesses and budding entrepreneurs is lagging behind.

### **Approach:**

- I. This Subgroup will focus their evaluations and recommendations on two areas: aid to existing small businesses and business start-ups.
- II. This Subgroup will examine the existing programs and initiatives and look at ways to improve workforce development, economic development and education in the Commonwealth.
- III. Establish a long term Strategic Plan to make Virginia the best state in which to own and operate a small business.

**Strategies:**

- I. Identify what programs Virginia offers to business start-ups and examine who is using them and who is not. Examine ways in which Virginia can increase exposure and access to more entrepreneurs.
- II. Examine what hurdles to small business creation the Commonwealth can remove or alter.
- III. Examine the programs that are available to existing small businesses and find what, if any improvements can be made.
- IV. Examine what tax code changes or incentives would spur small business growth and job creation.
- V. Consider how Virginia can improve and enhance its small business financial assistance programs and how to get more capital in the hands of small businesses.
- VI. Identify ways to consolidate entrepreneurship support and information.
- VII. Identify ways Virginia can work with its Congressional delegation to secure federal small business funding to be administered by the Virginia Small Business Financing Authority and the Virginia Capital Access Program (VCAP). Consider how Virginia can expand the opportunities to small and medium-size community banks.
- VIII. While Virginia is the #1 State for Business, we need to examine what will make Virginia the #1 State for Small Business.
- IX. Work with Workforce Development Subgroup and examine the workforce needs of Virginia's small businesses.
- X. Discuss promotion and expansion of the use of workplace-oriented education and training, including the use of registered apprenticeships.
- XI. Consider ways where Virginia can promote and expand the use of educational programs for employers.

**Initial Ideas and Recommendations:**

1. The budget of the DBA needs to be increased to a level more commensurate with the tax-paying constituency that the Department serves. DBA's budget has declined 56% over the past 8 years (2002-2010), including a 51% staff reduction over the past 4 years. Even with these drastic budget cuts, DBA has shown a 6 to 1 return on investment. By returning their funding to prior levels, we can leverage an even larger return on investment.
2. To help provide access to capital, consider the development of a Small Business Investment Tax Credit to expand early stage investments in targeted Virginia small businesses. The program may include provisions to provide tax credits to investors who make capital investment in certified small businesses.
3. DBA's status, funding, marketing and promotion needs to be elevated. Additionally, the consolidation of DBA under other economic development agencies, reduction of the department to sub-agency status, or any additional reduction of funding would further undermine the needs of the small business community.
4. The VSBFA needs more funding for its multiple loan and financing tools available to help Virginia entrepreneurs. Inadequate funding has left the Authority with little ability to help more than a handful of businesses. Businesses are turned away, not because they do not deserve help but because the programs are woefully underfunded.
5. Expand the types and sizes of companies eligible for state aid or support. Because of federal funding requirements, many of the incentive or loan programs are only available in specific regions of the state or for very specific purposes. The VSBFA needs additional revenue for the ability to be flexible in its financial programs.
6. Develop a model for grants to small businesses as long as they have the combined capability and infrastructure to define, manufacture, sell and support an innovative product or service. DBA would provide a grant up to 50% of the project budget referred to as a "Conditional Grant". The grant receiver is obligated to repay the DBA the total Conditional Grant received plus a small interest only from revenue generated by the product or service upon successful commercialization.
7. Virginia needs a statewide marketing campaign to promote the Commonwealth's small business friendly departments, programs and websites, as well as the other state sponsored educational opportunities available to the small business community. DBA's Business Information Services are some of the best kept secrets offered by the Commonwealth. This is due to a lack of marketing dollars available to promote the programs and resources the entrepreneurial community needs. Most state agencies offer quality education programs for employers, but without marketing support the constituency the programs are meant to help is unaware of the available aid.
8. Significantly enhance the "Virginia Business One Stop" website into a "First and Only Stop" by increasing the information, resources, and assistance available to Virginian entrepreneurs to ensure that truly only one stop is necessary to get a new business up

and running with minimal delay. Furthermore, Virginia needs to do a better job linking similar state and local requirements through Virginia's Business One Stop website so that information need be entered only once. Consider ways to address the issue of access fees as they turn away potential users. Communicate and coordinate with all state agencies and localities to ensure necessary forms and information are provided. Incentivize local governments to post business forms and required submissions in a searchable, easy-to-use format.

9. Promote Virginia as the "Best State in America to Open a Small Business." Much attention is given to the grand opening or relocation of Fortune 500 companies in Virginia but little is said about the many small businesses that thrive here. Virginians often hear about "mega projects," the Governor's Opportunity Fund, and the newest opening of a corporate headquarters, but we rarely hear about the accomplishments of the small business community even though small firms comprise the vast majority of businesses and the workforce.
10. Small business owners can often struggle to learn the state laws, rules and regulations. The creation of small business specific advisories to announce when state laws or regulations change would prove beneficial to small business owners.
  - Ex. The Small Business Advisory Act (Illinois). This act requires every State agency to make available on the internet a small business advisory page. The Illinois Attorney General uses the page to provide small businesses with a plain language explanation of any proposed or adopted rule or new legislation that affects small businesses. Explanations are posted for a minimum of 6 months. Small businesses are also directed to the State's Department of Commerce and First Stop Business Information Center, which operates as a central clearinghouse, notifying the small business community of each new rule or change in requirements affecting small businesses.
11. Create tax incentives to help our smallest firms hire employees or expand their locations/equipment. There are initiatives in a number of states that are being taken to encourage entrepreneurship. Some good policy initiatives enacted that have clear effects on entrepreneurs are:
  - Iowa adopted a capital gains exclusion for business sales.
  - Kansas cut property taxes.
  - Massachusetts slashed its tax rate on income and dividends.
  - Arizona, Delaware, Rhode Island and Wisconsin cut personal income taxes across the board, Maryland continued its personal income tax phase out, and New Mexico and Oklahoma cut the highest personal income tax rate.

Additional tax reform ideas include:

- Strategies to reform the BPOL tax. The BPOL tax, which is unfairly affects small businesses, is a detriment to economic development and job growth. Furthermore, the BPOL tax is structurally biased against start up businesses and effectively discourages businesses from selecting Virginia as a place to do business.

- Consider instituting the IRS model regarding fines for partnerships with less than 10 partners who pay on time.
  - Tax credit for advertising assistance.
  - Adding incentives for job creation by small businesses to help small employers such as a \$500/year unemployment tax credit for each unemployed Virginian hired or an income tax credit for each employer who keeps previously unemployed employee for 24 months.
  - Tax production and manufacture of digital content on cost of goods sold, not sales value, such as tangible goods.
  - Manufacturing equipment exempt from personal property tax.
12. The SRI report benchmarked Virginia's innovation foundations. Those benchmarks found that Virginia is average or weak in small business loans, business start-ups and entrepreneurship support. Compared to other benchmark states, (MD, GA, CA, FL, NY, MA, WA, NC, PA, and the US average) Virginia had the 2<sup>nd</sup> lowest level of entrepreneurs per capita in 2005 (220 per 100K population). The strategic focus for Virginia needs to be nurturing entrepreneurship and increasing access to capital.
  13. Improve customer service to entrepreneurs. Provide online approvals and prompt notifications to those who apply online. Allow for "fast track" fee based system for quick turnaround of licensing paperwork.
  14. Website needs to house the updated "How to Start or Expand a Business" guide in a format easily available for downloading and saving. Consolidate the following into one accessible guide:
    - a. Business Registration Guide from SCC
    - b. Virginia Guide to Establishing a Business from VEDP
    - c. A Guide to Business Incentives from VEDP
    - d. Guide to Local Taxes on Business from VEDP
  15. Help entrepreneurs identify and apply for small business grant programs. DBA should be fully focused on grants and provide training to grant writers. Furthermore, DBA should meet quarterly with the congressional liaison and discuss how they should be working to apply for and receive more grants.
  16. Assess small business community's workforce needs by category and training type to prevent one size fits all method.
  18. Identify strategies to help DOLI expand worker training and development. Continue the model of utilizing community colleges and regional education centers that provide classroom space and instructors by job classification..
  19. Develop public/private partnerships where larger businesses can mentor and partner with smaller businesses for worker training and development.

**Next Steps:**

In the interim, the staff and members of the Small Business Subgroup will continue to meet with interested parties soliciting ideas and examine other small business programs in competing states.

At our next meeting, Chris Chmura, President and Chief Economist for Chmura Economics & Analytics, a quantitative research, economic development and workforce consulting firm located in Richmond will present a recent study on the BPOL tax commissioned by the Virginia Retail Alliance.

The Subgroup will meet again on August 17th in Richmond to further consider initial recommendations followed by a September meeting to finalize a list of 8-10 recommendations to send to the Governor.